

# HAWAII PROCUREMENT INSTITUTE

April 27, 2004

## **Hawai'i Procurement Institute – Opinion Number 2004-01** **Policy Considerations Related To Exemptions From The Hawaii Procurement Code**

The Hawaii Procurement Institute respectfully submits comments on the procurement policy implications of exempting specified state agencies from coverage of the Hawaii Procurement Code (HRS Chapter 103D; the “Code”). For the reasons discussed below, exempting agencies from the Code will be unnecessary and, in the long run, potentially problematic for the administration.

Providing exemptions to individual agencies will impair the agencies’ ability to execute an efficient procurement program. Without the protections afforded in the Code, exempted agencies will be exposed to disruptive litigation that would necessarily be prevented by application of the Code. In addition, the exempted agencies may be required to assume the unnecessary and wasteful burden of drafting and maintaining separate procurement regulations instead of being able to use a single uniform set of regulations established under the Code.

Because the Code already provides for autonomy of contracting agencies, it is unnecessary to exempt any agency from the Code for the purpose of promoting autonomy or agency independence. Instead of promoting autonomy, exempting agencies from the Code will jeopardize uniform implementation of the protections against waste, fraud, and abuse the legislature placed in the Code. It will also potentially hinder the legislature in promoting and supporting specific segments of the Hawaii economy through preferential purchasing under the Code.

### A. Agency Exemptions Will Promote Disruptive And Wasteful Litigation

Among the principal purposes of any procurement code is the protection of agencies from disruptive litigation. Prior to Hawaii’s adoption of the Code, a losing contractor in a competition for award could contest the agency’s award to another contractor by suing either or both the agency and the winning contractor. *See Roberts Hawaii School Bus, Inc. v. Laupahoehoe Trans. Co.*, 91 Haw. 224, 928 P.2d 853 (1999) and *Brewer Environmental Industries, Inc. v. A.A.T. Chemical, Inc. and City and County of Honolulu, et al.*, 73 Haw. 344, 832 P.2d 276 (1992). Such suits are based upon the long established “right of a taxpayer to restrain a public officer from doing an illegal act. . . .” *Lucas v. The American-Hawaiian Engineering and Construction Co., Ltd*, 16 Haw. 80, 86 (1904).

The taxpayers’ right to enjoin award of a contract or have the court declare a contract invalid to prevent an “illegal act” was not limited to cases of fraud. *Federal Electric v. Fasi*, 56 Haw. 57, 527 P.2d 1284 (1974). Apart from clearly “illegal acts,” a disappointed contractor could sue on standard “protest” grounds of defective specifications or failure of an agency to promulgate

regulations authorizing the specific procurement mechanism used in the contract solicitation. *See Fasi*, 57 Haw. at 61.<sup>1</sup>

These “taxpayers’ suits” can prevent the award of a contract or result in the invalidation of an awarded contract. Even where the agency’s position is ultimately found justified, a taxpayer suit against a contract award can result in many years of delays and disruption of critical contracting actions. *See generally Roberts Hawaii School Bus, Inc. v. Laupahoehoe Trans. Co.*, 91 Haw. 224, 928 P.2d 853 (1999) (demonstrating that a 1990 solicitation for school bus services led to litigation lasting from 1993 until 1999).

Hawaii’s Code protects contracting agencies from these onerous taxpayer suits by providing an exclusive administrative protest procedure. *See* §§ 103D-701 & 704. Instead of permitting disappointed competitors to contest contract awards for years, the Code’s protest procedure imposes strict and short timelines to force prompt resolution of disappointed contractor complaints.

Specifically the Code requires filing of the protest no later than five days after notice of the alleged defect in the solicitation or award. *See* § 103D-701. Protests filed later than the five days set in the Code are untimely and may not be considered. *See* § 103D-701(a). For those protests filed within the required time period, the chief procurement officer of the agency will promptly determine the merits of the protest. *See* § 103D-701.

If the protester is dissatisfied with the chief procurement officer’s decision on the protest, the protester must apply for administrative review by an administrative law judge. *See* § 103D-709. The application for administrative review must be filed within seven days of the chief procurement officer’s final decision. *See* § 103D-712(a). The Code states that the administrative review will commence within twenty-one days of the request, and the Code empowers the administrative law judge to evaluate the evidence and issue a final and binding decision on the merits of the protest. *See* § 103D-709.

The Code provides that the agency’s contract award is stayed while the administrative review proceeding is pending. However, the stay may be avoided under the Code if necessary to protect public interests. The Code allows for continuation of contracting actions if the agency shows the needs of the government require the contracting action to go forward while the protest is resolved. *See* §§ 103D-709(e) & 701(f).

Because of the Code’s expedited protest procedures, the possible delays imposed under the Code are minimal. In comparison, the disruption created by taxpayer lawsuits can potentially

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<sup>1</sup> The Institute’s review indicates none of the currently exempt agencies have promulgated procurement regulations to support their independent procurement systems. The *Fasi* decision indicates the courts will invalidate contracts awarded by exempt agencies if these agencies have not issued rules and regulations to “insure fair and open competition among bidders” for the agency’s contracts. *See Fasi*, 57 Haw. at 61. Because these agencies are exempt from Chapter 103D, HRS, they may not be able to rely on the procurement regulations issued by the Procurement Policy Board pursuant to Chapter 103D, HRS.

extend for years, and a court injunction may be imposed to stop further agency contracting actions in the matter.<sup>2</sup>

If the agency prevails under the Code's administrative "protest" procedure, any stay of contracting action is lifted and the agency is allowed to go forward with its contract action. The protester may appeal by applying for judicial review, but the protester's application for judicial review will not further delay the agency. The Code specifically allows the agency to proceed with its contract work while the judicial review is undertaken. *See* §103D-710(b).

The Code's expedited administrative protest procedure is specifically intended to resolve complaints against contract awards promptly and prevent disruption of contracting by litigation. Although the Hawaii Supreme Court has never been asked to determine whether the Code's exclusive protest procedures will preempt and bar these taxpayer's suits, the Court has given a clear signal that the Code's provision will deprive disappointed contractors of the traditional taxpayer suit remedy. *See Roberts Hawaii* at n.11. Our analysis indicates that all complaints against contract solicitations or awards subject to the Code must be asserted under the Code's administrative protest procedures. If the protester attempts a taxpayer suit, the agency will be able to terminate the action against it immediately by demonstrating that the protester failed to exhaust its administrative remedies under the Code.

The "exhaustion of administrative remedies" defense will not be available to agencies exempt from the Code. If the legislature exempts an agency from the Code, the protester will not have the Code's administrative protest procedures as an available remedy, and the exempt agency will be subject to traditional taxpayer law suits challenging contract awards.

In light of the above, granting any agency an exemption from the Code will operate to expose the agency to the traditional taxpayer suits as the common law protest remedy. The Code's protections against these suits will apply only to agencies covered by the Code.

#### B. Universal Application Of The Procurement Code Will Not Limit Agency Autonomy

The Institute's understanding is that exemptions are thought to be necessary to promote independence and autonomy of procuring agencies. Because the Code already provides for agency autonomy, exemptions from the Code are not necessary. The Code is specifically crafted to provide each contracting agency the independence such exemptions are thought to serve.

The Code does nothing to limit agencies. It is modeled after the American Bar Association's 1979 Model Procurement Code, which was developed as the scholarly and professional standard for state procurement statutes. The Model Code was specifically designed to incorporate all legal tools necessary for a state to establish a fair, flexible, and reliable procurement system for statewide application. The Hawaii Code incorporates all the Model Code provisions that provide the maximum possible independence and flexibility for contracting agencies.

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<sup>2</sup> A taxpayer suit in the Circuit Court will likely also stay contracting actions. Because a taxpayer suit is specifically based upon a claim for a remedy to prevent an "illegal act," all such suits will include a demand to enjoin the agency from awarding or continuing performance on the contested contract.

In this context, the Code creates a broad range of specific mechanisms for the award of contracts. These mechanisms are time-tested methods for competing and awarding contracts in a manner: (1) calculated to protect taxpayer funds from waste and abuse and (2) designed to assure fair treatment of all contractors. The Federal government and virtually every State government use these same mechanisms to compete and award contracts.

Under the Code, agencies may elect to use sealed bidding or sealed proposals for competitive award of contracts. *See* §§ 103D-302 & 303. When purchasing professional services (other than human services covered under Chapter 103F), agencies can use standard merit-based selection procedures outlined in Section 103D-304. The Code also provides agencies authority to use streamlined procedures for emergency procurements and small purchases. *See* §§ 103D-307 & 305.

The only restriction the Code places on agencies is the general requirement that all state agencies must promote competition for their contracts and use sole sources only when fully justified. *See* §§ 103D-301 & 306. The Code's requirement to compete contracts is necessary to prevent the fraud, waste, and abuse of taxpayer funds that can occur when procurement officials direct awards to favored contractors.

Recent investigations into allegedly fraudulent, noncompetitive contract awards at the Honolulu Airport show the continuing risk of these kinds of abuses. The need to protect taxpayer dollars from potential abuse dictates that, barring extraordinary and justifiable circumstances, no government agency should be exempt from the Code's requirement to award contracts through fair and open competition.

Apart from the necessary restriction against noncompetitive contracts awards, the Code allows each agency to execute an independent contracting program under the supervision of the agency's own chief procurement officer. The various chief procurement officers are listed at Section 103D-203. The Judiciary, the Senate, the House of Representatives, and the various counties are among the independent agencies whose contracting programs are directed and controlled by each agency's "chief procurement officer" as designated under the Code. *See* § 103D-203.

By its own clear terms, the Code imposes no onerous limitations on agencies. Instead, it affords agency autonomy and independence through the designation of a chief procurement officer empowered to direct the agency's procurement program. There is no advantage in independence gained by exempting agencies from the Code because the Code already provides independence.

#### C. The Code Provides Exemptions for Special Needs Procurements

In those unique circumstances where competitive procurements under the Code are not advantageous to the government, the Code specifically allows for exemption of the procurements from Code provisions. Section 103D-102(b)(4)(L) empowers each agency's Chief Procurement Officer to exempt the special procurement requirement from the Code's competitive award rules. Accordingly, unique agency needs are already addressed in the Code, and a blanket exemption from the Code is not necessary.

D. Universal Application Of The Procurement Code Will Promote Legislative Programs to Improve the State Economy

The Code was crafted to allow the legislature to encourage and foster various industries within the State. Through the Code, the legislature has provided for the support of local small businesses. *See* §103D-901, *et seq.* In addition, the legislature has established “preferences” encouraging State and local government purchases of (1) products produced or grown within the State, § 103D-1002; (2) printing, binding, and stationary work performed within Hawaii, §103D-1003; (3) products containing recycled materials, §103D-1005; (4) software developed by Hawaii software development businesses, §103D-1006; and (5) services provided by nonprofit organizations serving and employing the disabled members of our community, §§103D-1009 through 1011.

The Code provisions defining “preferences” permits the legislature to promote specific segments of the State’s economy and encourage the development of new products and technologies. However, preference programs to enhance the State’s economy apply only to agencies subject to the Code. Agencies that are exempt from the Code are not subject to the legislature’s designated preferences. Even if the exempt agencies desired to implement the legislature’s preferences, they may be precluded unless they receive further legislative authorization and establish regulations defining the nature and scope of preferences to be applied in all competitive procurements. *See Fasi*, 57 Haw. at 61.

Under the circumstances, exempting specific agencies from the Code will impair the legislature’s ability to promote economic growth and encourage the development of new industries within the State. Expenditures by the exempt agencies will not be subject to the legislature’s preferences. As a result, there will be fewer dollars available to purchase products and services the legislature sought to promote when it established the various preferences in the Code.

E. Universal Application Of The Procurement Code Will Protect Against Abusive Practices The Legislature Sought to Eliminate

The Code also enables the legislature to impose specific requirements to eliminate practices the legislature believes are detrimental to the public’s perception of government procurement. For instance, the legislature imposed detailed procedural requirements on agency purchases of professional services when it passed Act 52 (2003).

In Act 52, the legislature amended Section 103D-304 to require that all contract awards to professional service providers be made based upon the merits of the provider and not upon any other factors. The legislature’s action in this case was to address a public perception that professional service contracts were sometimes awarded to companies based upon political affiliation or the amount of political contributions the companies had made to political leaders empowered to award the contracts.

By setting specific procedures for the evaluation of professional service providers eligible to receive the contract in question, the legislature eliminated the possibility that professional

services contracts could be used as a vehicle of political patronage. Such action assured the citizens of Hawaii that their tax dollars would not be used by politicians to reward cronies.

Granting specific agencies an exemption from the special Code provisions related to professional services contracts would operate to recreate the possibility of politically motivated contract awards. The result could be a return to the public perception that Hawaii's procurement system is corrupt and controlled by political operatives instead of by public servants charged with awarding contracts to the most qualified professional service providers.

F. Summary.

Based upon the preceding considerations, the Hawai'i Procurement Institute opines that exempting specific agencies from the Code is not in the best interest of the State government, its administration, the procurement community, and the general public. The Code establishes a time-tested, fair, and reliable set of mechanisms for the award of contracts using taxpayer dollars. The Code does not unduly limit agencies or prevent them from independently administering an efficient, autonomous, and flexible procurement program. To the extent agencies may need specific purchases to be exempted from Code requirements, the Code specifically provides for an exemption.

The Code also enables the legislature to assist specific local industries and only imposes those limitations needed to prevent waste of taxpayer dollars and abusive practices. Finally, the Code protects all agencies from suits that could disrupt and delay efficient conduct of the agency's procurement program. Under the circumstances, The Institute concludes that there is no compelling reason to exempt agencies from the Code; as well, granting blanket exemptions from the Code to individual agencies is not in the best interest of the State